PRICE-FIXING POLICIES OF THE FOOD ADMINISTRATION

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The short career of the Food Administration has resulted in revolutionizing, at least temporarily, the methods of marketing food products in the United States. Perhaps few economists who have not followed the bewildering succession of regulations, rulings, amendments, and substitutions which have succeeded one another from day to day, realize what a profound transformation has been worked in the nation's methods of carrying on the great business of food distribution. The price-fixing policies of the Food Administration have constituted striking experiments in a field heretofore confined largely to theory.[1]

At the outset it is important to make a distinction between basic price fixing and the regulation of prices by the control of margins. By the former is meant the actual fixing of price at any point in the line of distribution. Such a policy has a fundamental influence on the prices for which the commodity will be bought and sold at the various steps both preceding and succeeding the point at which price control is exercised. It is also clear that it tends to suspend to a considerable degree the influence of supply and demand on price, though not suspending the influence of price on supply and demand—a suspension that will be absolute at the point of price fixation, becoming less influential as the transaction is farther removed in the line of distribution from that point.

It is clear that merely fixing maximum margins for the several dealers who engage in the work of distribution may exercise some influence on the prices at which the product will be sold at the several stages of its movement; but the effect of this influence in restricting supply and demand ordinarily will be less weighty than that of basic price fixing.

Only in regard to a few classes of commodities has the Food Administration attempted to fix basic prices which suspend the

[1] The writer has had considerable opportunity to follow the development of the price-fixing policies of the Food Administration and, locally, at least, to observe some of their consequences. He has been Chairman of the Price-Interpreting Board for the city of Nashville and has had charge of this work for Tennessee.

direct influence of supply and demand on prices. Although the last mentioned kind of policy may be regarded as exceptional, rather than characteristic, in relation to the general aims of the Food Administration, it has attracted more attention and is better understood by the public than the more generally employed, though less radical, policy of controlling margins. Therefore, with the exception of a brief summary of the policy of basic price fixing, the greater part of the descriptive portion of this paper is devoted to the policies regulating margins.

Basic Price Fixing

Wheat is the only commodity of which the basic price has been determined absolutely and arbitrarily by government authority, although in several other instances, hereafter considered, basic prices have been established by agreements effected by the Food Administration with various agencies of production.

This exceptional policy with regard to wheat was especially provided for by Congress in the Food Control Act, the requirements of which are sufficiently familiar. In accordance with this enactment, the President, acting on the recommendation of the Food Administration, proclaimed a minimum price of $2.20 for number one northern wheat, Chicago basis. On this basic price a series of differentials was worked out for the various classes and grades and for the different primary and distributive centers of the United States. These prices have been extended to local markets by the subtraction or addition of the cost of shipment to or from the nearest large center, according to whether the locality is a surplus market or a deficit market for wheat.[2]

One important aspect of the policy has been that although designed originally to establish only a minimum price, it has actually resulted in the establishment of both a minimum and a maximum price, which are the same—that is, a practically invariable price. The necessity for this has arisen partly from the determination to prevent profiteering and partly from the fact that the complicated series of regulations with respect to the prices of wheat and the products thereof throughout the various stages of progress from producer to consumer made changes in the basic price difficult. For, not only has the Food Administration specified the exact margins that may be received by millers and dealers

[2] The basic price was subsequently changed to $2.26 on account of increase of freight rates, but in spite of continual political pressure, no further increase has been conceded.

for every important service in the manufacture and distribution of the several wheat products under various circumstances, but in the application of these regulations it has been the policy of the Administration to work out fair price schedules for each mill.

This price stability has been accomplished in several ways—partly by the judicial exercise of the enormous purchasing power of the Grain Corporation; partly by requesting the millers not to pay more than the minimum price for grain, at the same time agreeing to rebuy from the millers at a fair price all grain held by them in the event that the market was flooded by imports after the close of the war.[3]

As already noted, the policy of basic price fixing has been extended beyond the specific authorization by Congress—but undoubtedly in conformity with the spirit of the Food Control Act—by the policy of agreements effected by the Food Administration with producers.

In the case of sugar, the government had little power to fix prices to the producer of the raw commodity, for a large part of the domestic supply is obtained by importation, and prices for the domestic product are largely based on the price of the portion of the supply which is imported.[4] However, although the arrangements with the beet sugar factories, the Cuban and Louisiana sugar factories, and the sugar refiners have been made matters of agreement, the Food Administration has the power to regulate the margin received for manufacture except in the case of the foreign establishments.

These agreements have resulted approximately in fixing the farm prices, for the prices paid farmers for sugar beets and for sugar cane are largely dependent on the mill price of raw sugar, although the relation is more direct in the case of sugar cane, so far as American producers are concerned.[5]

After the base prices for the raw product were determined, the Administration was free to control the prices asked by refiners and subsequent dealers by virtue of the authority to prevent excessive

[3] "America's Grain Trade," address delivered by Herbert Hoover at the conference of representatives of the grain trade of the United States with the Food Administration Grain Corporation, New York, April 30 to May 1, 1918.

[4] The details of the agreements concerning sugar were so fully set forth by Professor Roy G. Blakey in a recent article that the present writer considers it unnecessary to repeat them. See *Quarterly Journal of Economics,* Aug., 1918.

[5] On account of the fact that contracts for the purchase of cane are based on a sliding scale varying directly with the price of sugar.

margins of profit. The result of the exercise of these powers has been the same as in the case of wheat. Practically unvarying prices have been established with differentials for costs of transportation from refinery or import centers to different centers of distribution, and fixed margins of profits for the various dealers in the trade. These prices have been changed only under authorization of the Food Administration. In consequence the retail price of sugar throughout the United States during the past year has been established at about 9 to 10 cents a pound, a price that has not been seriously affected by the extreme variations in supply that have occurred during that period.

A further extension of the policy of price-fixing by agreement has recently been made in respect to certain packing-house products. On August 16, 1918, the Food Administration held a conference with some forty packers who receive allotments of government export business. A schedule of prices for hams, bacon, and lard was agreed upon. Since the important packers of the country are included in the agreement, it is certain that the agreed prices will at least constitute a maximum which may not be exceeded by other packers.[6]

The effect of these agreements for the fixing of prices on manufactured food products is indirectly and within broad limits to determine prices paid to farmers—as, for instance, the prices of sugar beets and hogs. In the case of rice, however, the Administration has gone one step farther and effected an agreement as to the prices to be paid by rice mills to farmers. A less extreme proceeding is the agreements concerning the prices of prunes and raisins effected with the growers' organizations.

The Control of Dealers' Margins

The regulation of dealers' margins is based on the clause in section four of the Food Control Act whereby it is declared unlawful to "make any unjust or unreasonable rate or charge." The Food Administration has amplified this dictum by forbidding licensees to impose any "unjust, exorbitant, unreasonable,

[6] Circular letter 6-H-816, August 23, 1918. This arrangement has been revoked since the present paper was prepared.

Temporary agreements have also been effected with large dealers in cold storage eggs and poultry. Such an agreement effective in the large centers of distribution was arranged to continue until the spring of 1918. W. F. Gephart, "Perishable Produce under Food Regulation," *Quarterly Journal of Economics,* Aug., 1918, p. 625.

discriminatory, or unfair commission, profit, or storage charge."[7]

A considerable body of rules, both general and specific, for the definition of fair margin has been developed. These rules are unique both in their character and effect.

The general principle first adopted was that a margin is limited to a "reasonable advance over the actual purchase price of the particular goods sold without regard to market or replacement value."[8] This rule was subsequently modified so that "purchase price" read "average purchase price of all lots of the same grade and size of the same commodity in his possession or invoiced to him, not contracted to be sold."[9] This modification has to do with the determination of the basic price to which the "reasonable margin is to be added."

Considerable progress has been made in determining the meaning of the "average purchase price." "Purchase price" is not used in the literal sense of the net invoice price of the goods, but includes freight to the public railway terminal in the dealer's own town. When the dealer operates several branches, the "purchase price" must be figured separately for each branch.[10] For butter, eggs, and poultry, when placed in cold storage, the "purchase price," or cost, includes original buying price, transportation charges, storage charges, insurance charges, interest on the money invested at the current rates, during the period of storage, and actual cost of printing when butter is put in print form from tubs or cubes.[11]

Since it is clearly impossible for the dealer to calculate separately the purchase price of each particular lot of goods added to his stock and keep the same distinct as a basis of determining fair prices, he is allowed the alternative of averaging the "purchase price" of all goods of the same kind and grade. In the case of cold storage commodities only the goods placed in storage during a period of one month may be averaged. It is left optional with the dealer whether he shall average the "purchase price" of different brands that are of the same grade and size.[12]

[7] *General License Regulations,* I-A-5.

[8] *Maximum Margins on Sales by Wholesalers to* (1) *Retailers,* (2) *Importers of Beans and Peas,* (3) *Merchandise Brokers,* April 6, 1918.

[9] *Special License Regulations,* XI-A-S.

[10] *Special License Regulations,* XI-A-5-Note, and XI-A-5 a.

[11] *Special Rules and Regulations Governing Dealers in Cold Storage Eggs and Frozen Poultry, effective March 2, 1918; Special Regulations Governing Manufacturers, Dealers, Brokers, and Commission Merchants in Butter,* July 19, 1918.

[12] *Special License Regulations,* XI-A-5-and note.

In effecting the average, the "purchase price" of each lot bought is weighted according to the quantity, and the average purchase price of all goods on hand, weighted according to the quantity, is averaged with the purchase price of new lots similarly weighted.

It will be obvious that so long as the average is honestly effected it can not be used to increase the dealer's margin of profit provided the dealer observes the rules respecting the margin of profit. If, for instance, his margin per barrel is 50 cents, he would make the same gross profit whether he averaged or did not average the several lots. However, averaging will affect the level of price at which he sells, and his decision to average or not to average is likely to be determined by the state of the market and the policy of his competitors. However, in the case of butter, eggs, and poultry placed in cold storage, if the dealer averages any of the commodity put in cold storage during a given month, he must average all of the commodity placed in storage during that month.[13]

When no specific margin has been laid down by the Food Administration, the standard of reasonableness is the profit which the "dealer customarily enjoyed on the same commodity in the prewar period on an even market under freely competitive conditions."[14] Indeed, in theory this standard is applicable even when the maximum is specified. It was expressly stated that even the maximum margins specified by the Food Administration should be regarded as "guides only," and should not be considered to limit the general principle that the advance must be reasonable in relation to the customary prewar profit of the individual. In the very next sentence, however, it is asserted that "high margins, even if customary during prewar period, are not justifiable now."[15]

The confusion is evident. If the reasonable margin is the customary margin enjoyed by the particular individual in the prewar period, but an unreasonable margin in the prewar period may not be taken as a point of departure, we are thrown back on the problem of determining what was reasonable in the prewar period. In the next paragraph of the same document from which the above excerpts are quoted, an attempt is made to meet this difficulty by the assertion that "the reasonable margin for any particular dealer depends upon his cost of operation." Cost of oper-

13 *Special License Regulations*, XX; *Special Regulations Governing Wholesalers, Retailers, and All Other Dealers in Cold Storage Eggs*, July 23, 1918.

14 *Maximum Margins on Sales by Wholesalers to Retailers, etc.*, April 6, 1918.

15 *Ibid.*

ation refers not to the general cost of operation but to the costs assignable to the sale of the particular class of commodity. Moreover, it undoubtedly indicates present cost, and not cost in the prewar period.

It will be clear that only a little progress has been made in determining what is a reasonable margin, for, assuming that the costs of operation have been properly allocated to the particular class of commodity under consideration—a difficult accounting problem and one which the Food Administration has frankly refrained from undertaking[16]—no criterion has been furnished by which to determine how much net profit the dealer should be allowed on the particular commodity.

There are evidences that it was intended to use the total net profit of the business in relation to the net profit for the prewar business as a means of deciding the question of "reasonable advances." In fact, the monthly reports which licensees were required to make until May 1, 1918, included the data necessary to determine the actual net profit of the business as a whole, as well as the margins on specific lots of commodities sold. It is apparent, however, that this would be a difficult standard to apply, and it is certain that little effort was made to apply it. So far as the writer knows, the expression "prewar period" has not been specifically interpreted. We do not know whether it refers to a single year or a group of years. If a business was operated at a loss in the prewar period, there is no reason why its losses should be perpetuated. On the other hand, as we have noted, the Food Administration has specifically declared that "high margins, even if customary during the prewar period, are not justifiable now."

The preceding analysis of the theoretical standards of fair price developed by the Food Administration may suggest a vacillating and confused mode of application. As a matter of fact, however, this has not been true. The accuracy of definition and definiteness of formulation requisite for rate regulation in peace times under the constant tests of the courts have not been neces-

[16] "Neither, the Food Administration nor any other branch of the government has prescribed uniform cost accounting systems for either wholesale or retail food distributors. The government has not, therefore, indicated how the licensee, in dealing with a commodity covered by the reasonable profit rule, shall dispose of cartage, interest, or other special charges; but it does expressly forbid the employment of such charges with the purpose, or with the effect, of increasing the licensee's profit above his own reasonable prewar level." *Special License Regulations,* XI-A-5-Note.

sary during the present emergency. On the one hand, there has been little disposition on the part of dealers to dispute the policies and decisions of the Administration; on the other hand, the Administration has been liberal in the enforcement of its policies. In general, it has been found impossible to deal with each individual on the basis of the status of his present business in relation to the prewar business. As a matter of fact, it appears that the Washington authorities were swamped with the monthly reports, and found it impossible to give them all the minute examination that was requisite to apply closely the theoretical standard of fair profit, not to mention the even greater difficulty of determining the prewar status of the business. Indeed, the congestion became so great that after May 1, 1918, the Administration abandoned the policy of requiring the detailed monthly reports from licensees.[17]

As a matter of fact, the Food Administration has developed specific maximum margins for the majority of the licensed commodities. These margins are determined largely according to the prewar standards customary in the trade. Little effort appears to have been made to compel the individual dealer to sell at a margin less than the maximum specific margin, irrespective of the relation of his present profits to his prewar profits. In general, only failure to abide by this maximum has been considered as "prima facie evidence" of a violation of the regulation governing fair profits. Consequently the regulations, as enforced, are not based on the net profit of the sale of a particular class of goods by the individual dealer, and they have an even more remote relationship to the net profit of the individual business as a whole.

With a few exceptions, specific margins for each class of wholesale dealer have been developed for wholesale dealers in practically all kinds of food commodities. Among the exceptions are fresh vegetables and fruits, live poultry, fresh meats, and fresh eggs. Margins have been fixed for dressed poultry, eggs, and butter, in cold storage, and, by a recent ruling, for fresh butter. Manufacturers' margins also have been fixed in the case of a number of important commodities, including the principal mill products and sugar. Cold storage warehousemen are required to report their rates for storage to the Food Administration, and changes can be made only by obtaining the consent of the authorities.

The Food Administration looks askance at discrimination in

[17] Circular letter, 6-H-612, June 12, 1918.

price as between individual customers. Usually, when maximum margins are specified, no distinction is made between credit and cash sales. Even when the reason for discrimination is due to the size of the order, discrimination is likely to be regarded as unreasonable. However, such discrimination is permitted in the case of some commodities. Thus, on mill products the margin varies according to whether the sale is in car lots, ton lots but less than car lots, or less than ton lots. It is probable that this makes possible considerable evasion through breaking up large orders into small units. For non-perishable groceries there is usually no variation in margin according to the amount sold, except that when original packages are broken the licensee is allowed the actual cost of repacking, not exceeding 5 per cent.[18]

The fixing of maximum margins would be of no effect as a regulative measure if dealers were left free to buy and sell the same commodity as many times as they pleased, for it would be easy to gain the speculative advantages of a rising market by selling to a colleague or confederate, or by selling and repurchasing at the selling price for subsequent resale. The Food Administration has attempted to prevent this evasion of its maximum margins by a series of regulations based on the cardinal principle that commodities must be kept "moving to the consumer in as direct a line as practicable and without unreasonable delay."[19]

However, there are a number of circumstances under which it is necessary for one distributor to resell to another dealer of the same rank in the line of distribution. The main principles involved in this aspect of food control may be illustrated by the general rules governing resales of non-perishable groceries.[20] The Food Administration recognizes several kinds of transactions in which a resale may result in a total margin of profit for both sales exceeding the maximum allowed for one sale. For example, a wholesaler who buys in carload lots may distribute the same among other wholesalers who for some good reason are unable to buy direct from the source of supply or who can not purchase in carload lots. The same privilege is granted a wholesaler who enjoys special or exclusive privileges of cold-storage warehousing. Likewise, a wholesaler may sell surplus stocks of goods bought in good faith for the service of his trade, which he has been un-

[18] *Special Regulations,* XI-A-5, Note.

[19] *Special License Regulations,* XI-A-5, Note.

[20] Excluding sugar and mill products.

able to dispose of, the fact that he has warehoused the goods being an evidence of good faith. In all the above cases the first seller is permitted not more than one-half the maximum margin allowed for a single sale direct to retailers, while the second seller can add only the lowest of the margins allowed for that particular commodity. Only one such resale is permitted. The second seller must dispose of his goods to the retailer or consumers. Accommodation sales among dealers, known in the trade as "pick-ups," are permitted provided the two parties divide the usual margin allowed for a single sale.[21]

Likewise, regulations have been developed to prevent the taking of excessive margins by short-circuiting in the regular line of distribution while retaining the regular margins allowed, or by combination sales—that is, selling two or more commodities at a lump price.[22]

Control of Retail Prices

In November, 1917, the Food Administration inaugurated the policy of establishing "price-interpreting boards" in the principal centers of population. In May, 1918, the plan was enlarged with the view of establishing a price-interpreting board in each county of the United States. The boards are composed of representatives from wholesalers, retailers, and consumers.[23] In some states the organization is much more complete than in others.

The list of fair maximum prices thus determined is published weekly in local papers. It is also reported to Washington and to state headquarters. It is customary to quote prices that retailers must pay to wholesalers, as well as the prices to consumers. Because of the rapid spread of "cash and carry" stores, it is generally necessary to publish two sets of retail prices.

The Food Administration has sent to the chairman of local boards a list of retail price margins. These margins, however, serve merely as a guide for the local board. The latter is instructed not to exceed the maximum margin except when the circumstances are unusual, and not at all in the case of bread, butter, flour, sugar, and eggs.

21 *Special License Regulations,* XI-A-5-Note, continued, (2).

22 *Special Rules and Regulations Governing Dealers in Cold Storage and Frozen Poultry,* effective March 2, 1918.

General License Regulations, 1-A-23 (a). Exception is made for combination sales of substitutes for wheat flour.

23 Circular Letter 6-H-529, May 17, 1918.

Legally the price-interpreting boards have no power to fix prices, for, with exception of those commodities for which basic prices have been determined by law or by agreement, the Food Administration's power over prices does not extend beyond the determination and interpretation of reasonable margins of profit for food manufacturers and dealers. If price-interpreting boards could fix retail prices, this would substantially amount to the fixing of wholesale prices, and, within narrower limits, would largely control the prices of farm products used for food. At most, the price-interpreting boards merely determine what prices are to be regarded as fair under existing local conditions. If a dealer exceeds the prices so determined, this may constitute a presumption of unfairness which will justify investigation.

As a matter of fact, the determination of prices by price-interpreting boards has had the approximate effect of fixing maximum prices, for local food administrators frequently regard the infraction of the published prices as evidence of unfairness.

Results and Conclusions

It is perhaps too early to attempt a conclusive statement of the results of the price-fixing policies outlined above. However, some of the results of the policy are now apparent, and the writer ventures to combine these facts with certain *a priori* observations.

In the first place, the experience of the Food Administration appears to indicate that effective government control of competitive prices of products of wide consumption is not only entirely possible, but subject to difficulties less formidable than economists have generally believed.

The surprising facility in enforcement of these policies may be attributable in part to a united sentiment of patriotism, further strengthened in its effect by a universal public condemnation of "profiteering." However, the real success has been due to the exceptional powers bestowed on the Food Administration. The power to license food manufacturers and distributors has conferred practically autocratic authority within the purposes of the law. As principal agency for coördinating purchases of food for government use and for exportation, the Administration has occupied so preponderant a position in the markets of the country that through its buying power alone it has been able to regulate prices, partly through purchases and sales and partly through using its power of purchase to induce dealers to conform to its

policies. Finally, as in its negotiations with Cuban sugar producers, the Administration has been able to rely on the international prestige of the government which it represents.

One of the most obvious effects of the policy of regulating dealers' margins is that it suspends the tendency toward a single price within the market. It is true that in ordinary times this is only a tendency, and from ignorance, inertia, and other conditions, the prevalence of a single price, even in wholesale transactions, has not been so general as sometimes may be indicated by discussions of value theory.

Whatever the prevalence of the one-price tendency in normal times, it is certain that the result of the margining policy described above has been to produce many different prices for the same commodity in the same market. Suppose that dealer "A" bought rice at 8 cents a pound, "B" purchased at 9 cents, "C" at 7½ cents, and so on; ordinarily, if the demand is strong enough to require the entire supply, the price will tend to be high enough to enable "B" to sell at a profit, the other more fortunate dealers making a still larger conjunctural profit. If the market is not immediately strong enough to justify so high a price, "C" will hold his fortunate purchase until the market advances. On the contrary, if the market weakens the price may be determined according to "C's" buying price, while his unfortunate competitors must suffer a speculative loss. However, when dealers are limited to a maximum margin, "C" can gain no more than his fixed margin by waiting, while, on the contrary, he risks a possible decline on the market. Consequently, he will be inclined to sell for enough to enable him to obtain his maximum margin. His less fortunate competitors have the option of selling at less than the margin—possibly even at less than cost—or of waiting until the low-price supply is exhausted, on the chance that the market may go higher.

It is quite possible that the market may decline still further, in which case the high-cost dealers will be even more out of pocket, besides incurring the trouble and delay of holding. However, during the present emergency the general tendency of prices has been upward. Consequently the normal situation in the market has been that the fortunate dealers who have on hand a supply purchased at a low cost occupy the center of the stage until the supply is exhausted, while their competitors calmly wait until the time when their high-cost supply may be sold at a fair margin of profit.

In the fixing of retail prices, however, there is necessarily a return to the one-price policy. Obviously a retail price-interpreting board, confronted with a considerable variety of whosesale prices in the same market, may be puzzled to know what price may be regarded as the normal basis of retail prices. In Tennessee the state food administration has determined that the lowest cost that will supply the market for the time being shall be the basis on which retail prices shall be determined. When the low-cost supply is exhausted, then the price may be increased to the point that will make possible the sale of an adequate supply.

However, when the policy of regulating margins is supplemented by a policy of basic price fixing, the lack of uniformity in wholesale and retail prices is considerably reduced, for a start is made from a uniform base, and a base that fluctuates at infrequent intervals. This has been true of sugar and flour.

One result of the margining policy is to eliminate the motive for speculation. A dealer can gain no more than his maximum margin when the market advances, while he must suffer a heavy loss when the market declines. It is doubtful if the Food Administration could have maintained this policy of unlimited loss and limited gains except in a time like the present when the normal movement of prices is upward.

One of the indirect consequences of the policy of controlling margins is the stimulation of independence and discrimination in buying, especially on the part of retailers. Since there may be many prices in the market instead of a uniform price, the dealer finds it no longer profitable to buy always from one or two dealers. The retailer who, on account of poor credit or for other reasons, must buy largely from one jobber is indeed in a sorry plight. From another standpoint, however, it has been true that during the present emergency there has been less necessity for care in buying. The continuous advance in prices has assured the dealer that sooner or later he may expect to obtain the margin allowed by the Food Administration.

A fundamental problem of price fixing is to determine the price that is just high enough to call forth sufficient supply to meet demand. When a uniform price is established, the price must be high enough to induce the marginal producer to furnish his portion of the supply. Such a price bestows a surplus return upon the producers whose expenses are lower than the expenses of the marginal producer. However, this merely results in giving legal

sanction to surplus incomes which would normally exist under ordinary conditions of competition.

In the determination of basic prices the Food Administration has followed the above-mentioned principle, striving to make the price high enough so that production might be in no way discouraged, even erring, if necessary, on the side of liberality.[24] For instance, the prices of beet sugar and of cane sugar were deliberately established at the level that would cover the expenses of the least efficient producers, although in the former case the range of cost was from $4 to $7 per ton.[25]

For regulating prices charged by wholesale distributors of food commodities the Food Administration seized the other horn of the dilemma by abandoning the policy of uniform price, substituting the regulation of dealers' margins, as described above, in order to eliminate excessive profits. Even in the regulation of margins, however, it has been necessary to make specific margins high enough to cover the expenses of the least efficient distributors —those with small turnover and high operating expense—besides a fair amount over for safety. Consequently the writer has found it to be the general opinion among dealers of his acquaintance that the margins fixed by the Food Administration are very generous. Moreover, in the interpretation of retail prices the efficient retailer is enabled to earn a considerable surplus in order that the inefficient retailer may not be forced out of business.

Recently another mode of escaping entirely from the well-known dilemma described above has been employed. A Sugar Equalization Board has been formed with a capital of $5,000,000 with the purpose to "absorb the high peaks of cost in sugar production and to make a small margin on the low cost of certain foreign sugars which may be purchased and thus secure an equalization of the price to the public on a lower level than will otherwise be possible."[26] In other words, the government acts as an equalizing agency whereby price is made uniform, while producers, regard-

[24] However, the Food Administration has from the first repudiated the idea of high price as an incentive to economy in consumption. See Thomas H. Dickinson, "A Year of Food Administration," *North American Review,* July, 1918.

[25] See Roy G. Blakey, "Sugar Prices and Distribution under Food Control," *loc. cit.*

[26] *Ibid.*

less of relative efficiency, are paid merely on the basis of cost plus fair profit.[27]

As a form of governmental control of competitive prices this method appears to offer a means of avoiding the disadvantages of other methods of price control by making possible uniform prices at lower levels than would obtain under freely competitive conditions. The method is clearly impossible as a means of controlling the price of wheat and other farm staples, because it would be necessary to ascertain the individual costs of hundreds of thousands of producers. However, even for such commodities the method might be used to equalize regional differential surpluses.

We now may venture to consider dispassionately the advantages and disadvantages of price control as a permanent policy, in the light of our new experience.

One of the immediate effects of price fixing in the case of wheat was to suspend speculation in futures on the boards of trade at the same time that the usefulness of such speculation was destroyed. The principal economic functions of such speculation have been to provide a means of hedging and to eliminate extremes of fluctuation by discounting future changes in conditions.[28] The stabilization of prices obviously renders these functions unnecessary.

It has long been a problem of deep concern how speculation might be eliminated without losing its economic advantages. There can be no doubt that the general sentiment of the country is overwhelmingly against organized speculation. The average citizen understands little of its advantages, and it is not easy to make him comprehend them. The consuming classes are inclined to attribute a large part of the cost of living to speculation on the organized exchanges, while the farmer is firmly convinced that they absorb a large part of his profit. Therefore, the elimination

[27] President Van Hise recently suggested this method for the regulation of coal prices. *Conservation and Regulation in the United States during the World War,* prepared for the United States Food Administration. Coal prices are now based on individual mine costs plus a fair profit, without attempting to maintain uniform price.

[28] It is not conclusively established that the effect of organized speculation is to reduce the magnitude of temporal price variations. Certain other advantages incidentally facilitated by organized speculation—namely, elimination of unnatural price differentials between localities and the creation of a wide, sensitive, and continuous market—may conceivably be effected by spot transactions without the aid of futures.

of the more important advantages of speculation by price stabilization is justified, at least in part, by the very positive advantage of allaying this long-established source of popular suspicion and discontent.

Price stabilization undoubtedly involves another positive economic advantage. It is undoubtedly true that farming is an exceedingly precarious industry, combining the uncertainties both of the weather and of prices. This precariousness becomes more apparent to the degree that the industry develops from self-sufficiency into commercial and capitalistic farming. The elimination of fluctuations in price after the crop is produced and the guaranty of price in advance of the crop season would reduce greatly the uncertainties of agricultural production and remove an important source of rural discontent. To some extent, also, a greater degree of certainty may be introduced into the business of manufacturing food products—now partially effected by hedging—as well as in the processes of distribution.

The disadvantages and difficulties of price control appear exceedingly formidable in statement, especially when basic price fixing is involved. It may be worth while to estimate their relative importance.

One of the most apparent is the impossibility of controlling prices—especially of farm products—without the process becoming a bone of political contention. The recent tremendous pressure for increasing wheat prices is a very convincing reminder of this danger—a danger which, to the writer's mind, constitutes the greatest objection to a policy of price fixing. However, the danger might be somewhat reduced by a definitely announced policy of balancing in the long run government losses and gains in the process of equalization.

Theoretically, it would be exceedingly difficult for government authorities to calculate a year and a half ahead what price will maintain the existing acreage and also insure the full consumption of a crop of very uncertain quantity. However, there are several mitigations of this difficulty. If the price is fixed too high, the government will find it impossible to dispose of the entire amount in domestic consumption. It would be possible to pay the farmer the guaranteed price and to lower the price to consumers, the government bearing the loss temporarily in the hope of making it up when conditions are more favorable. However, at the time the farmers begin selling their crops it is not always clear that the

reduction of price will be necessary. It is true, it would be difficult to lower prices after a part of the product has passed into the hands of manufacturers and distributors, without serious complications. In any case, the government can export the surplus, even though it may be necessary to do so at a loss. If the price is fixed too low, it may have the effect of discouraging production. This may or may not result in a crop too small to meet the normal consumption of the country, depending on weather conditions and other physical factors. If the crop should prove inadequate, authorities may resort to imports, although at a possible loss. It should not be forgotten, too, that difficulties mentioned above are considerably reduced by the reserve carried forward from one crop season to the next. This may be employed as a shock absorber. Supplemented by an intelligent control of imports and exports, it may be used to modify the effects of temporary or seasonal fluctuations in demand and supply.

Another difficulty is the effect of price fixing on the inter-relations of different commodities. Some farm commodities are used in the production of others. Certain products are substitutes for others, either in production or in final consumption. Even when prices are determined by competition these relationships are continually disturbed by frequent price variations. It is this fact, for instance, that makes the business of fattening beef cattle one of extreme risk. Fixed prices would make the conditions of productive use and substitution stable for a considerable period of time so that the producer could know what to count upon, and govern his action accordingly.

It appears that the principal advantage of leaving these relationships to be affected by competition is that, in case the normal relationship is seriously impaired by price changes, variations will occur in demand which will exert a more or less powerful influence toward restoring prices to the usual relationship. Thus, if corn rises in price so much that farmers cannot afford to feed it to cattle, the demand for corn for this purpose will decline. The reduction in demand may aid in lowering the price to the point that will enable feeders to resume its use. However, the use of corn for beef cattle constitutes only one of many sources of demand, which may prove so inelastic in other directions that the restoration of usual conditions will not be effected. In fact, under competition prices vary more largely on account of substantial alterations in supply due to weather, insects, and crop diseases,

both at home and abroad, than to any nice adjustment to relative food values or interdependent cost relationships.

The establishment of accurate price differentials between localities is a problem of great, though not insuperable, difficulty. There are large areas which are practically always surplus areas tributary to a particular primary market. Prices merely reflect prices in the primary market less the expense of shipment. Other large areas are always consuming markets, whose prices reflect closely the changes in a particular distributing market. Regions characterized by the above-mentioned conditions offer no peculiar difficulty in the determination of price differentials.

In many localities, however, the problems of establishing differentials according to location are not so simple. There are some regions which have a surplus in one year and a deficit in other years, according to the success of the crop. Again, there are regions which have a surplus in one season and a deficit at another season of the year. Barring miscalculations, however, this need occur only for products that cannot be stored. There are producing regions which do not always ship to the same primary market, the direction of shipment depending on variations of prices in different local markets. Such regions are located on the divides separating different market watersheds. Finally, there are consuming regions which do not draw supplies continuously from the same distribution market.

In statement the above variations sound exceedingly formidable. For the determination of prices, however, it is clear that the difficulty arises in connection with the attempt to maintain a uniform price level everywhere with necessary adjustments for local differences in supply as dependent on costs of shipment. Consequently, in a policy of price fixing involving a uniform price level to farmers followed by the regulation of dealers' margins, the necessity of regulating local differentials arises only at the stage when the uniform level is maintained—that is, the paying price to the farmers. After the commodity leaves the farmers' hands, price-fixing responsibility requires only the regulation of dealers' margins, leaving to the play of competition the adjustment of supply and demand between localities.

There has been much discussion of late concerning costs as a basis for the determination of agricultural prices—a discussion that has been brought to a head by the milk wars in New York and Chicago. The controversy has centered about the difficulties

of determining costs, especially the question whether products such as grain and hay used for feeding dairy cattle shall be counted in the final costs at their market value or at their actual cost of production.[29] As a problem of accounting, the question has but one answer: the accurate determination of the costs of a final result are possible only if intermediate processes are rated at their actual costs, and not at their values at the time of use.

Such an answer, however, does not settle the problem of public policy in price fixing, for such a policy is one of valuation—a question of fairness, not a question of methods of accounting. That materials produced by a business enterprise and used in the production of a subsequent commodity by the same enterprise should be reckoned at cost of production, and not at market value, is no proof that the resulting sum of costs is a fair basis of valuation, and assuredly it does not establish it as an expedient basis.

In the view of the present writer, a policy of agricultural price fixing should be opportunist and eclectic. As in the problem of determining railway rates, no single formula is adequate. The very difficulties of exact cost accounting are a proof of its inadequacy, especially in view of the fact that the costs of different producers vary widely. It is doubtful if any arrangement could be devised that would serve to determine in practice the location of marginal cost, even if conditions were static. Since the margin is constantly varying with changes in the volume of demand and the length of time under consideration, as well as because of alterations in methods of production and changes in the values of the various factors of production, it seems probable that cost would be even more remotely influential in agricultural price fixing than in railway rate-making.

It appears that an agricultural price must be high enough to induce producers to plant the acreage or keep the number of cows that experience has shown will furnish a certain quantity of the commodity under average seasonal conditions. The primary question must be what quantity is required. Obviously, the aim is not to satisfy demand, for demand varies with price. The problem is one of deciding what quantity will meet the normal needs of the country or region to be supplied. The second prob-

[29] *Cf.* especially H. C. Taylor, "Price-Fixing and the Cost of Farm Products," *Bulletin 292*, Agricultural Experiment Station of the University of Wisconsin; C. S. Duncan, "The Chicago Milk Inquiry," *Journal of Political Economy,* XXVI, Apr., 1918.

lem is to ascertain what price will cause the requisite acreage to be planted. Whether this price equals, exceeds, or falls short of the expense of production to so-called marginal producers, will be indicated by the result. It is doubtful if estimates of cost would serve as anything more than a general guide, indicating the general limits of policy. For particular years many producers may be sub-marginal or, conceivably, all may be super-marginal, according to the product per acre as determined by seasonal fluctuations, and it is not always the largest crop nor the highest price that brings the farmer the largest returns.

The writer is not convinced of the immediate desirability of permanent governmental control of the prices of staple foods, but he believes that our present experiences have demonstrated that the policy is not so absurd and impossible as many economists have been wont to believe. At any rate, the desirability of such control must be considered separately for each particular commodity, for the special merits of the policy will vary in each case, and the special difficulties will not be the same for all commodities.